

January 11, 2010
Ms. Mary Nichols, Chair
California Air Resources Board
1001 I Street
Sacramento, CA 95814

RE: CALCHAMBER COMMENTS ON THE PRELIMINARY DRAFT REGULATION FOR A CALIFORNIA GREENHOUSE GAS CAP-AND-TRADE PROGRAM

Dear Ms. Nichols:

Thank you for the opportunity to comment on the California Air Resources Board's (CARB) 'Preliminary Draft Regulation (PDR) for a California Greenhouse Gas Cap-and-Trade Program' that was released on November 24, 2009.

The California Chamber of Commerce (CalChamber) is the largest, broad-based business advocate in the state, representing the interests of over 16,000 California businesses, both large and small. CalChamber has been a constructive voice throughout the process of implementing AB 32 (The Global Warming Solutions Act) and continues to do so in order to ensure that the greenhouse gas emission reductions required are achieved while maintaining the competitiveness of California businesses and the health of the economy.

Unfortunately, our ability to comment on the PDR is limited due to the fact that key policy decisions – those constituting some of the most controversial elements of a future cap and trade program – are omitted from the draft. Absent a determination on critical issues such as allowance distribution, availability and use of offsets, and linkages with future national and international cap and trade programs, we cannot comment effectively on the merits of the future program as outlined in the PDR. Such forthcoming policy decisions will prove critical to determining the overall success of the cap and trade program and whether or not California can meet its greenhouse gas reduction goals in a cost-effective manner, as required by AB 32.

CalChamber believes that for a successful and cost-effective cap and trade program to be implemented, the auctioning of allowances must be kept at de minimis levels in order to avoid the serious cost impacts that would accompany full auctioning and be borne by California businesses and consumers. To illustrate, CARB's Economic and Allocation Advisory Committee (EAAC) has estimated that if allowance prices reach \$60 by 2020 under a 100% auction system, California businesses would have to pay \$143 billion between 2012 and 2020 just to continue operating in the state. Such an outcome is unacceptable. More cost-effective approaches to achieving our AB 32 goals must be taken if California is to maintain its position as a leader in combating climate change.

CalChamber maintains its position that a successful cap and trade program should not be a California-only unilateral approach but should instead allow for seamless linkages with other national and international programs from the outset. Additionally, we believe that a well-designed program should include a broader use of offsets than the 4% limit detailed in the PDR and that real, verifiable offsets should not be limited geographically. Finally, we do not believe it is necessary to accelerate the inclusion of transportation fuels from 2015 to 2012 as pondered in the PDR. In fact we believe CARB must first

analyze the potential impacts, especially the economic impacts of bringing fuels into the cap and trade program before developing regulations to do so.

The above-mentioned policy decisions will be paramount to determining the success or failure of California's cap and trade program and will provide a strong indication to the business community, consumers, and other stakeholders of CARB's commitment to cost-effective implementation so that it can meet AB 32's dual goals of environmental protection and economic prosperity.

Allowance Allocation

One of the most controversial aspects of designing the cap and trade program lies with the EAAC's recommendation of the allocation method for allowances. While the EAAC has yet to make a final recommendation, it has come to our attention that officials are considering a full 100% auction of allowances. As described above, such a policy choice could cost California businesses \$143 billion between 2012 and 2020. Ostensibly, the burden of these fees would be paid by large employers, utilities and public institutions such as University of California, Department of Water Resources and local water and sanitation districts. We strongly feel that a complete and thorough economic analysis of the impacts that a 100% auction would have on California is necessary prior to any final adoption. This is particularly important given the current realities of high unemployment and severe state and local budget deficits.

Linkage with Other Programs

With federal cap and trade legislation currently stalled in Congress and California standing as the only state in the Western Climate Initiative (WCI) to have an enforceable greenhouse gas emissions cap on its economy, California stands alone on the brink of developing a cap and trade program. This California-only cap and trade program negates the opportunity for economic growth, and instead puts California at significant economic risk. The CalChamber is concerned that a unilaterally designed program could end up costing significantly more to the state's consumers and businesses by discarding the advantages associated with full integration into a potential federal program and future international programs. Furthermore, a unilateral approach poses a leakage threat, undermining the dual environmental and economic purpose of the program. Beyond the leakage potential, the economic risks also include a decline in the overall business climate in California which is also aggravated by the current recession. Though slated for implementation in 2012, the uncertainty of future AB 32 compliance costs – including those realized under a cap and trade program – are influencing the decisions made by California businesses today.

Maximizing Offsets

The AB 32 Scoping Plan discusses the need for offsets and recognizes that there should not be regional boundaries for their use if the offsets are real and verifiable. In fact, according to the Scoping Plan, "High quality offset projects located outside of California can help lower compliance costs in California while reducing GHG emissions in areas that would otherwise lack the resources needed to do so." (Page 37). Under the current PDR, however, CARB staff recommends severely restricting the use of offsets to 4%. This limitation is overly restrictive and contrary to the intent of the Scoping Plan as a 4% offset cap does little to minimize upfront cost impacts that would be experienced under a cap and trade program. Prior research has shown that maximizing the use of offsets would be one of the most effective tools for reducing program costs while still achieving the greenhouse gas reduction goals of AB 32.

Transportation Fuels

CalChamber is concerned about accelerating the transportation fuel date within the cap and trade program from 2015 to 2012, especially since it is unclear how gasoline and diesel fuels will be treated under the Low Carbon Fuel Standard (LCFS). We believe that the additional impacts of cap and trade requirements on fuel supply and affordability should be better understood before moving up the inclusion of fuels under the cap and trade program. Given the importance of transportation on California's economy, and the importance of energy costs to nearly every resident and business in the state, it is imperative that CARB does a thorough analysis of the economic impact of fuel inclusions in the cap and trade program; making sure that costs are minimal and total benefits to California are maximized.

Further, we believe that addressing the inclusion of transportation fuels and natural gas in the 2015 timeframe allows California time to transition the cap and trade program to include fuels. Failure to adopt the most cost-effective policies could have significant adverse impacts to the state with California businesses and consumers bearing a substantial financial burden.

Legal Issues

Several analyses, including a paper released by CARB's own EAAC Legal Issues Sub-Committee in November 2009, reveal the serious legal challenges that will likely constrain CARB's ability to generate revenues from the regulated community beyond those specifically authorized in the AB 32 statute. CalChamber agrees with several of the issues raised in the November EAAC analysis, including the referenced expert legal opinions that argue "the state may not collect [General Fund] or any revenue through an auction" without additional statutory authorization. Additionally, CalChamber agrees with the November analysis in that Sinclair "appears to pose significant barriers" to many of the proposed uses of AB 32-related revenues. Finally, AB 32 author Fabian Nunez's clarifying letter states unambiguously that the intent of AB 32 is not to raise revenues for purposes beyond covering the administrative costs of the program. It stated: "it is my intent that any funds provided by Health & Safety Code Section 38597 are to be used solely for the direct costs incurred in administering this division". This letter strongly suggests that an auction system or other revenue-raising mechanism would be directly contrary to the legislative intent of AB 32. In conclusion, we do not believe you have the legal authority to adopt revenues beyond those for a reasonable charge for administrative activities.

Again, we appreciate your consideration of these comments. We would be happy to discuss any issues or concerns further with you as implementation proceeds.

Sincerely,



Brenda Coleman
Policy Advocate

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